

**State Funding Board
Sewage Treatment Facilities Fund**

**For the Year Ended
June 30, 2000**

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**STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY**

State Capitol
Nashville, Tennessee 37243-0260
(615) 741-2501

John G. Morgan
Comptroller

January 31, 2001

The Honorable Don Sundquist, Governor
and

Members of the General Assembly
State Capitol
Nashville, Tennessee 37243

and
Members of the State Funding Board
State Capitol
Nashville, Tennessee 37243

Ladies and Gentlemen:

Transmitted herewith is the financial and compliance audit of the State Funding Board, Sewage Treatment Facilities Fund, for the year ended June 30, 2000. You will note from the independent auditor's report that an unqualified opinion was given on the fairness of the presentation of the financial statements.

Consideration of internal control over financial reporting and tests of compliance resulted in no audit findings.

Sincerely,

John G. Morgan
Comptroller of the Treasury

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State of Tennessee

Audit Highlights

Comptroller of the Treasury

Division of State Audit

Financial and Compliance Audit
State Funding Board
Sewage Treatment Facilities Fund
For the Year Ended June 30, 2000

AUDIT OBJECTIVES

The objectives of the audit were to consider the fund's internal control over financial reporting; to determine compliance with certain provisions of laws, regulations, and contracts; to determine the fairness of the presentation of the financial statements; and to recommend appropriate actions to correct any deficiencies.

AUDIT FINDINGS

The audit report contains no findings.

OPINION ON THE FINANCIAL STATEMENTS

The opinion on the financial statements is unqualified.

"Audit Highlights" is a summary of the audit report. To obtain the complete audit report, which contains all findings, recommendations, and management comments, please contact

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**Audit Report
State Funding Board
Sewage Treatment Facilities Fund
For the Year Ended June 30, 2000**

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State Funding Board Sewage Treatment Facilities Fund For the Year Ended June 30, 2000

INTRODUCTION

POST-AUDIT AUTHORITY

This is a report on the financial and compliance audit of the State Funding Board, Sewage Treatment Facilities Fund. The audit was conducted pursuant to Section 4-3-304, *Tennessee Code Annotated*, which authorizes the Department of Audit to “perform currently a post-audit of all accounts and other financial records of the state government, and of any department, institution, office, or agency thereof in accordance with generally accepted auditing standards and in accordance with such procedures as may be established by the comptroller.”

Section 8-4-109, *Tennessee Code Annotated*, authorizes the Comptroller of the Treasury to audit any books and records of any governmental entity that handles public funds when the Comptroller considers an audit to be necessary or appropriate.

BACKGROUND

The Sewage Treatment Facilities Fund has operated since the early 1970s under authority of Section 68-221-202, *Tennessee Code Annotated*. The fund provided financial assistance to local governments and utility districts for the construction of sewage treatment, solid waste recovery, and waterworks facilities. A user’s fee was authorized to generate funds for the borrowing entities to repay the loans. General obligation bonds were sold to finance the program. Although these bonds remain full faith and credit obligations of the state, they are being retired from resources of the fund. Financing for this program is currently generated by the Tennessee Local Development Authority.

ORGANIZATION

The State Funding Board approved contracts for program financing after state environmentalists provided engineering expertise to determine the eligibility and priority of municipal projects. The State Funding Board is composed of the Governor, who serves *ex officio* as chairman; the State Treasurer; the Secretary of State; the Commissioner of Finance and Administration; and the Comptroller of the Treasury, who serves *ex officio* as secretary.

The staff of the State Funding Board is composed of certain employees of the Division of Bond Finance, Office of the Comptroller of the Treasury.

An organization chart for the State Funding Board is on the following page.

AUDIT SCOPE

The audit was limited to the period July 1, 1999, through June 30, 2000, and was conducted in accordance with generally accepted government auditing standards. Financial statements are presented for the year ended June 30, 2000, and for comparative purposes, the year ended June 30, 1999. The State Funding Board, Sewage Treatment Facilities Fund, forms an integral part of state government and as such has been included as an enterprise fund in the *Tennessee Comprehensive Annual Financial Report*.

The audit covered fund 33 of the State of Tennessee Accounting and Reporting System (allotment code 307.07).

OBJECTIVES OF THE AUDIT

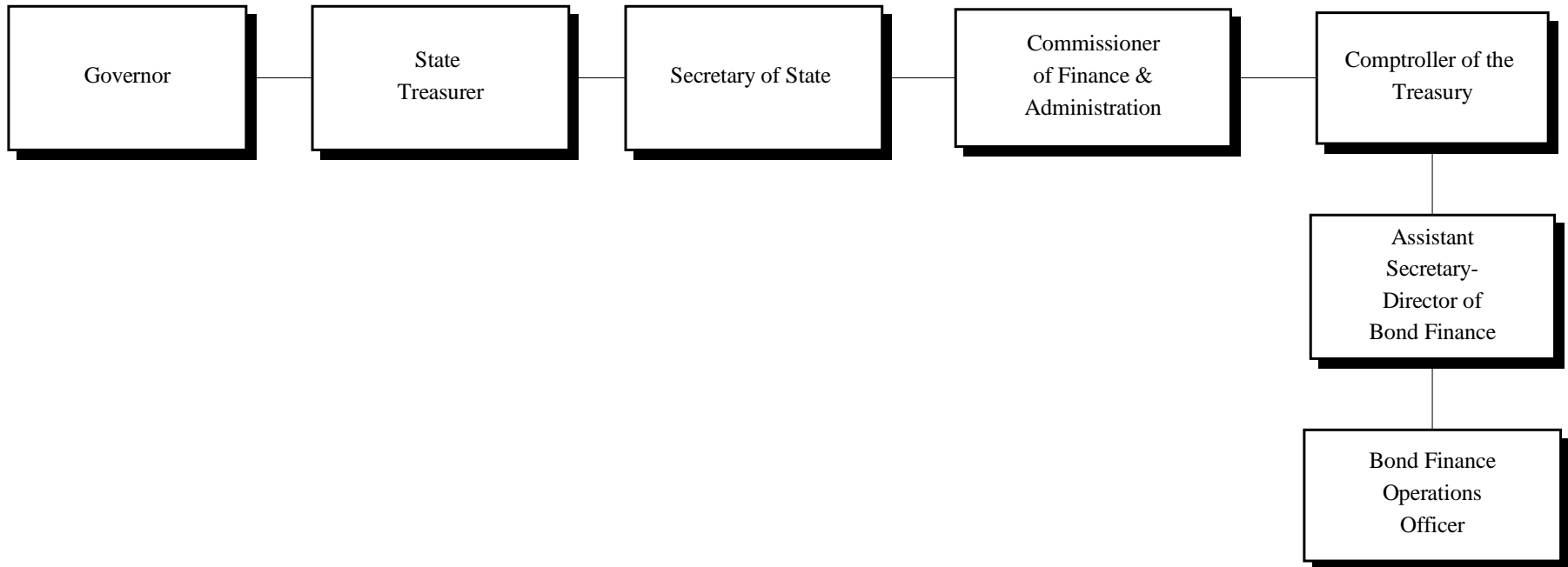
The objectives of the audit were

1. to consider the fund's internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements;
2. to determine compliance with certain provisions of laws, regulations, and contracts;
3. to determine the fairness of the presentation of the financial statements; and
4. to recommend appropriate actions to correct any deficiencies.

PRIOR AUDIT FINDINGS

There were no findings in the prior audit report.

TENNESSEE STATE FUNDING BOARD ORGANIZATION CHART



RESULTS OF THE AUDIT

AUDIT CONCLUSIONS

Internal Control

As part of the audit of the financial statements for the year ended June 30, 2000, for the State Funding Board, Sewage Treatment Facilities Fund, we considered internal control over financial reporting to determine auditing procedures for the purpose of expressing an opinion on the financial statements, as required by generally accepted government auditing standards. Consideration of internal control over financial reporting disclosed no material weaknesses.

Compliance

The results of our audit tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

Fairness of Financial Statement Presentation

The Division of State Audit has rendered an unqualified opinion on the financial statements of the State Funding Board, Sewage Treatment Facilities Fund.



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DEPARTMENT OF AUDIT
DIVISION OF STATE AUDIT
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**Report on Compliance and on Internal Control
Over Financial Reporting Based on an Audit of
Financial Statements Performed in Accordance With
*Government Auditing Standards***

November 29, 2000

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the financial statements of the State Funding Board, Sewage Treatment Facilities Fund, as of and for the year ended June 30, 2000, and have issued our report thereon dated November 29, 2000. We conducted our audit in accordance with generally accepted government auditing standards.

Compliance

As part of obtaining reasonable assurance about whether the fund's financial statements are free of material misstatement, we performed tests of the fund's compliance with certain provisions of laws, regulations, and contracts, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit, and accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance that are required to be reported under *Government Auditing Standards*.

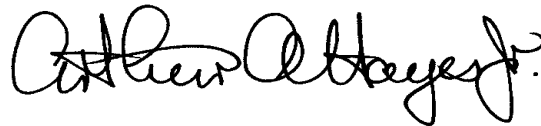
The Honorable John G. Morgan
November 29, 2000
Page Two

Internal Control Over Financial Reporting

In planning and performing our audit, we considered the fund's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control over financial reporting that might be material weaknesses. A material weakness is a condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. We noted no matters involving the internal control over financial reporting and its operation that we consider to be material weaknesses.

This report is intended solely for the information and use of the General Assembly of the State of Tennessee and management and is not intended to be and should not be used by anyone other than these specified parties. However, this report is a matter of public record.

Sincerely,

A handwritten signature in black ink, reading "Arthur A. Hayes, Jr." in a cursive script.

Arthur A. Hayes, Jr., CPA, Director
Division of State Audit

AAH/ks



**STATE OF TENNESSEE
COMPTROLLER OF THE TREASURY
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Independent Auditor's Report

November 29, 2000

The Honorable John G. Morgan
Comptroller of the Treasury
State Capitol
Nashville, Tennessee 37243

Dear Mr. Morgan:

We have audited the accompanying balance sheets of the State Funding Board, Sewage Treatment Facilities Fund, as of June 30, 2000, and June 30, 1999, and the related statements of revenues, expenses, and changes in retained earnings and cash flows for the years then ended. These financial statements are the responsibility of the fund's management. Our responsibility is to express an opinion on these financial statements, based on our audits.

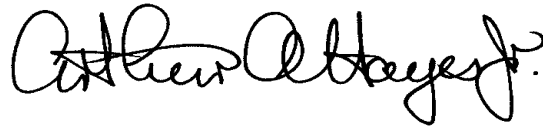
We conducted our audits in accordance with generally accepted government auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of the State Funding Board, Sewage Treatment Facilities Fund, as of June 30, 2000, and June 30, 1999, and the results of its operations and cash flows for the years then ended in conformity with generally accepted accounting principles.

The Honorable John G. Morgan
November 29, 2000
Page Two

In accordance with *Government Auditing Standards*, we have also issued our report dated November 29, 2000, on our consideration of the fund's internal control over financial reporting and our tests of its compliance with certain provisions of laws, regulations, and contracts. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

Sincerely,

A handwritten signature in black ink, reading "Arthur A. Hayes, Jr." with a stylized flourish at the end.

Arthur A. Hayes, Jr., CPA, Director
Division of State Audit

AAH/ks

STATE FUNDING BOARD
SEWAGE TREATMENT FACILITIES FUND
BALANCE SHEETS
JUNE 30, 2000, AND JUNE 30, 1999

(Expressed in Thousands)

	<u>June 30, 2000</u>	<u>June 30, 1999</u>
<u>ASSETS</u>		
Current assets:		
Cash (Note 2)	\$ 3,790	\$ 3,801
Loans receivable	3,125	3,195
Interest receivable	<u>1</u>	<u>1</u>
Total current assets	<u>6,916</u>	<u>6,997</u>
Other assets:		
Loans receivable	17,797	21,055
Deferred charges	<u>101</u>	<u>112</u>
Total other assets	<u>17,898</u>	<u>21,167</u>
Total assets	<u><u>\$ 24,814</u></u>	<u><u>\$ 28,164</u></u>
<u>LIABILITIES AND EQUITY</u>		
Liabilities:		
Current liabilities:		
Accrued interest payable	\$ 335	\$ 388
Due to local governments (Note 3)	450	444
General obligation bonds payable, net (Note 4)	<u>3,125</u>	<u>3,195</u>
Total current liabilities	<u>3,910</u>	<u>4,027</u>
Noncurrent liabilities:		
General obligation bonds payable, net (Note 4)	<u>17,222</u>	<u>20,356</u>
Total liabilities	<u>21,132</u>	<u>24,383</u>
Equity:		
Retained earnings, unreserved	<u>3,682</u>	<u>3,781</u>
Total liabilities and equity	<u><u>\$ 24,814</u></u>	<u><u>\$ 28,164</u></u>

The Notes to the Financial Statements are an integral part of this statement.

STATE FUNDING BOARD
SEWAGE TREATMENT FACILITIES FUND
STATEMENTS OF REVENUES, EXPENSES, AND CHANGES IN RETAINED EARNINGS
FOR THE YEARS ENDED JUNE 30, 2000, AND JUNE 30, 1999

(Expressed in Thousands)

	Year Ended <u>June 30, 2000</u>	Year Ended <u>June 30, 1999</u>
OPERATING REVENUES		
Revenue from loans	\$ 817	\$ 983
Investment income	<u>236</u>	<u>216</u>
Total operating revenues	<u>1,053</u>	<u>1,199</u>
OPERATING EXPENSES		
Interest expense	1,102	1,257
Administrative expense	15	24
Bond issuance costs	<u>10</u>	<u>10</u>
Total operating expenses	<u>1,127</u>	<u>1,291</u>
Operating loss	<u>(74)</u>	<u>(92)</u>
Operating transfer to Tennessee Local Development Authority	<u>(25)</u>	<u>(25)</u>
Net loss	<u>(99)</u>	<u>(117)</u>
Retained earnings, July 1	<u>3,781</u>	<u>3,898</u>
Retained earnings, June 30	<u><u>\$ 3,682</u></u>	<u><u>\$ 3,781</u></u>

The Notes to the Financial Statements are an integral part of this statement.

STATE FUNDING BOARD
SEWAGE TREATMENT FACILITIES FUND
STATEMENTS OF CASH FLOWS
FOR THE YEARS ENDED JUNE 30, 2000, AND JUNE 30, 1999

(Expressed in Thousands)		
	Year Ended June 30, 2000	Year Ended June 30, 1999
Cash flows from operating activities:		
Operating loss	\$ (74)	\$ (92)
Adjustments to reconcile operating loss to net cash used by operating activities:		
Amortization	10	10
Revenue from loans	(817)	(983)
Investment income	(236)	(216)
Interest expense	1,102	1,257
Increase (decrease) in due to local governments	6	(10)
Total adjustments	65	58
Net cash used by operating activities	(9)	(34)
Cash flows from noncapital financing activities:		
Principal payments	(3,195)	(3,045)
Interest paid	(1,164)	(1,316)
Operating transfer to Tennessee Local Development Authority	(25)	(25)
Net cash used by noncapital financing activities	(4,384)	(4,386)
Cash flows from investing activities:		
Collections of loan principal	3,329	3,119
Interest received on loans	817	1,125
Interest received on investments	236	216
Net cash provided by investing activities	4,382	4,460
Net increase (decrease) in cash	(11)	40
Cash, July 1	3,801	3,761
Cash, June 30	\$ 3,790	\$ 3,801

The Notes to the Financial Statements are an integral part of this statement.

**State Funding Board
Sewage Treatment Facilities Fund
Notes to the Financial Statements
June 30, 2000, and June 30, 1999**

NOTE 1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Reporting Entity

The Sewage Treatment Facilities Fund was created to provide financial assistance to local governments and utility districts through the issuance of state general obligation bonds. The Tennessee Local Development Authority currently generates the financing for the program. Pursuant to the Governmental Accounting Standards Board's *Codification of Governmental Accounting and Financial Reporting Standards*, Section 2100, the State Funding Board, Sewage Treatment Facilities Fund, is part of the primary government and has been included in the *Tennessee Comprehensive Annual Financial Report* as an enterprise fund (State Loan Program).

Basis of Presentation

The accompanying financial statements have been prepared in conformity with generally accepted accounting principles as prescribed by the Governmental Accounting Standards Board (GASB). The State Funding Board, Sewage Treatment Facilities Fund, follows all applicable GASB pronouncements as well as applicable private sector pronouncements issued on or before November 30, 1989.

Measurement Focus and Basis of Accounting

The accompanying financial statements have been prepared using the accrual basis of accounting and the flow of economic resources measurement focus. Under this basis, revenues are recorded when earned, and expenses are recorded at the time liabilities are incurred.

Bond Premiums, Issuance Costs, and Refunding Costs

Bond premiums, issuance costs, and refunding costs are deferred and amortized over the life of the bonds using the straight-line method. Bonds payable are reported net of the applicable unamortized bond premium and refunding costs. Unamortized issuance costs are reported as deferred charges.

State Funding Board
Sewage Treatment Facilities Fund
Notes to the Financial Statements (Cont.)
June 30, 2000, and June 30, 1999

NOTE 2. DEPOSITS

The fund had \$3,790,459 in the State Treasurer's pooled investment fund at June 30, 2000, and \$3,801,200 at June 30, 1999.

The pooled investment fund administered by the State Treasurer is authorized by state statute to invest funds in accordance with policy guidelines approved by the State Funding Board. The current resolution of that board gives the Treasurer authority to invest in collateralized certificates of deposit in authorized state depositories, prime commercial paper, prime bankers' acceptances, certain repurchase agreements, various U.S. Treasury and agency obligations, limited money market mutual funds, and obligations of the State of Tennessee pursuant to *Tennessee Code Annotated*, Section 9-4-602(b). The pooled investment fund is also authorized to enter into securities lending agreements in which U.S. government securities may be loaned for a fee. The loaned securities are transferred to the borrower by the custodial agent upon simultaneous receipt of collateral securities. The State Treasurer's pooled investment fund's custodial credit risk is presented in the *Tennessee Comprehensive Annual Financial Report*.

NOTE 3. DUE TO LOCAL GOVERNMENTS

This account represents loan principal overpayments and interest earnings that will be refunded to local governments.

NOTE 4. BONDS PAYABLE

Bonds payable at June 30, 2000, and June 30, 1999, are as follows (expressed in thousands):

	<u>June 30, 2000</u>	<u>June 30, 1999</u>
General obligation bonds, 5.0%, issued March 1, 1977, due in generally decreasing amounts of principal and interest ranging from \$2.5 million in 2001 to \$0.7 million in 2006	\$10,035	\$11,980

State Funding Board
Sewage Treatment Facilities Fund
Notes to the Financial Statements (Cont.)
June 30, 2000, and June 30, 1999

Refunding general obligation bonds, 4.6% to 5.0%, issued February 15, 1996, due in various amounts of principal and interest from \$1.6 million in 2001 to \$1.0 million in 2010 (net of unamortized premium of \$280 and deferred amount on refunding of \$193 at June 30, 2000, and net of unamortized premium of \$309 and deferred amount on refunding of \$213 at June 30, 1999)	<u>10,312</u>	<u>11,571</u>
Total bonds payable	<u>\$20,347</u>	<u>\$23,551</u>

Debt service requirements to maturity for all bonds payable at June 30, 2000, are as follows (expressed in thousands):

For the Year(s) <u>Ending June 30</u>	<u>Principal</u>	<u>Interest</u>	<u>Total</u>
2001	\$ 3,125	\$1,004	\$ 4,129
2002	3,280	848	4,128
2003	2,845	684	3,529
2004	2,990	542	3,532
2005	2,830	392	3,222
2006-2010	<u>5,190</u>	<u>685</u>	<u>5,875</u>
Total	<u>\$20,260</u>	<u>\$4,155</u>	<u>\$24,415</u>